

Mbhashe Municipality

Audit Report

REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON MBHASHE LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Mbhashe Local Municipality (the municipality) set out on pages xx to xxx, which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No.56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the General Notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Property, plant and equipment

6. I was unable to obtain sufficient appropriate audit evidence for the completeness of infrastructure assets as a number of rural roads and community halls are not on the asset register. I was unable to confirm the completeness by alternative means. Consequently I was unable to determine whether any adjustments relating to the movable tangible assets

stated at R118 million (2012: R134.4 million) in note 7 to the financial statements was necessary.

Irregular expenditure

7. Section 125(2) of the MFMA requires the financial statements of the municipality to disclose material irregular expenditure that occurred during the financial year end. Audited payments amounting to R1.2million (2012:R0) were irregular, as they were made in contravention of the supply chain management (SCM) requirements. These amounts were not included in the irregular expenditure disclosed in note 28 to the financial statements. Consequently, the irregular expenditure disclosed is understated by at least this amount. However, it was not practicable to determine the full extent of the understatement, as there was no system of control operating throughout the financial year to identify the completeness thereof.

Prior year cash flow statement

8. I was unable to obtain sufficient appropriate audit evidence for the presentation of the prior year cash flow statement, as the line item other non cash items amounting to R 4,4 million is unsubstantiated. I was unable to confirm the accuracy of this amount by alternative means. Consequently I was unable to determine whether any adjustments relating to the prior year cash flow line item other non cash items amounting to R 4,4 million was necessary.

Qualified opinion

9. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Mbhashe Local Municipality as at 30 June 2013 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

10. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

11. As disclosed in note 36 to the financial statements, the corresponding figures for 30 June 2012 have been restated as a result of an error discovered during the current financial year in the financial statements of the municipality at, and for the year ended, 30 June 2013.

Material under spending of Conditional grants

12. The municipality has materially under spent on the Municipal Infrastructure Grant (MIG). Unspent conditional grant for the MIG amounts to R 12million(30%) as at 30 June 2013

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

13. In accordance with the PAA and the General Notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

14. I performed procedures to obtain evidence about the usefulness and reliability of the

information in the annual performance report as set out on pages ... to ... of the annual report.

15. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development priorities. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information*.
16. The reliability of the information in respect of the selected development priorities is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
17. The material findings are as follows:

Usefulness of information

Presentation

18. Improvement measures in the annual performance report for a total 17 (100%) of the planned targets not achieved were not disclosed as required by section 46 of the Municipal Systems Act. This was due to an inadequate review of the presentation of the annual performance report by management

Reliability of selected development priorities in the annual performance report

Basis for adverse conclusion

19. The FMPPI requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The information presented with respect to Development Priority: Basic Service Delivery and Infrastructure Investment, was not reliable when compared to the source information and/or evidence provided. This was due to the lack of standard operating procedures for the accurate recording of actual achievements and lack of adequate review of the validity of reported achievements against source documentation.

Additional matter

20. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Achievement of planned targets

21. The municipality did not achieve 47% of its planned targets during the year. This is due to inadequate performance management systems in place and as well as the lack of capacity in the municipality.

Compliance with laws and regulations

22. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the General Notice issued in terms of the PAA are as follows:

Strategic planning and performance management

23. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the Municipal Systems Act. This is due to the fact that no performance assessments were performed during the year.
24. The municipality did not have and maintain effective, efficient and transparent systems of financial and risk management and internal controls as required by section 62(1)(c)(i) of the Municipal Finance Management Act.

Annual financial statements, performance and annual reports

25. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements of current liabilities identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.
26. Oversight report, containing comments on the annual report, was not adopted by council within two months from the date on which the 2011/12 annual report was tabled, as required by section 129(1) of the Municipal Finance Management Act.
27. The council's oversight report on the 2011/12 annual report was not made public within seven days of its adoption, as required by section 129(3) of the Municipal Finance Management Act.

Audit Committee

28. A performance audit committee was not in place and the audit committee was not used to fulfil the performance audit committee function, as required by Municipal planning and performance management regulation 14(2)(a).

Internal audit

29. The internal audit did not audit the results of performance measurements, as required by section 45(1)(a) of the Municipal Systems Act and Municipal planning and performance management regulation 14(1)(a).
30. The internal audit unit did not audit the performance measurements on a continuous basis and submitted quarterly reports on their audits to the municipal manager and the performance audit committee], as required by Municipal planning and performance management regulation 14(1)(c). This was due to the fact that the quarterly performance reports were not prepared for all the quarters during the financial year under audit

Procurement and contract management

31. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).

Human resource management and compensation

32. The competencies of financial and supply chain management officials were not assessed in a timely manner in order to identify and address gaps in competency levels as required by the Municipal Regulations on Minimum Competency Levels regulation 13.

33. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury as required by the Regulations on Minimum Competency Levels reg14(2)(a).
34. Senior officials were appointed in acting positions for a period of more than six months, in contravention of section 56(1)(c) of the Municipal Systems Act.
35. The municipality did not develop and adopt appropriate systems (policies) and procedures to monitor measure and evaluate performance of staff in contravention of MSA sec 67(d).
36. The senior managers directly accountable to the municipal manager did not sign performance agreements, as required by section 57(2)(a) Municipal Systems Act.

Expenditure management

37. Reasonable steps were not taken to prevent irregular expenditure, fruitless and wasteful expenditure, as required by section 62(1)(d) of the Municipal Finance Management Act.

Revenue Management

38. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the Municipal Finance and Management Act.

Asset management and liability management

39. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the Municipal Finance Management Act.

Internal control

40. I considered internal control relevant to my audit of the financial statements and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for the qualified opinion, the findings on the predetermined objectives and the findings on compliance with laws and regulations included in this report.

Leadership

41. The municipality was not able to achieve stability of leadership during the current year and audit, as the executive was replaced, key management suspended and personnel were acting in senior positions. This resulted in a lack of oversight as sufficient monitoring controls to ensure proper implementation of policies at an operational level and that the audit action plan was fully addressed.
42. The municipality has not developed adequate policies and procedures to address the collection, recording, processing, monitoring and reporting on predetermined objectives. Consequently the annual performance report was not useful or reliable

Financial and performance management

43. The reliance by management on both the consultants and the audit process to achieve fair presentation did not create a sustainable platform for achieving clean administration. The systems for assets, unspent grants and irregular expenditure was not kept up to date and verified during the year had to be corrected during the audit process
44. The municipality did not have a proper system of record management that provides for the

maintenance of information that supports the reported information contained in the annual performance report. This includes information which relates to the collection, collation, verification, storing and reporting of actual performance information. As a result the annual performance report was not useful or reliable.

45. The entity did not have adequate processes and assignment of responsibilities to ensure compliance with all applicable laws and regulations. As a result, there were instances of non-compliance with the MFMA and DoRA
46. The systems underlying the procurement processes at the municipality were inadequate to prevent and detect irregular expenditure on contracts entered into, resulting in irregular expenditure that was disclosed in the accounting records of the municipality. Effective and appropriate disciplinary steps were not taken against officials who made and permitted unauthorised, irregular and fruitless and wasteful expenditure.

Governance

47. Although internal audit and audit committee meet regularly throughout the year, they were not effective in strengthening the control environment within the municipality as material misstatements in the AFS, performance report and material non-compliance findings were identified during the audit.
48. The audit committee and the internal audit function did not adequately report on the performance management system or performance reports throughout the financial year under review. The municipality thus lost the benefit that may have been obtained had these reports been completed.

Auditor-General
East London

29 November 2013



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence